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C O N F I D E N T I A L SECTION 01 OF 02 LUANDA 000648

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FOR AF/S AND EAP/CM

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TAGS: ELTN ETRD EFIN EPET PINR CH AO
SUBJECT: ANGOLA: WORK STOPS ON THE MALANJE RAILROAD

LUANDA 00000648 001.2 OF 002

Classified By: Ambassador Cynthia G. Efird. Reason 1.4 (b) and (d)

¶1. (C) Summary. Work has apparently stopped along the railroad line linking Luanda and Malanje with Chinese railroad workers claiming they have not been paid for eight months. At the root of the problem is the nature of the deal between China International Fund (CIF) a private Hong Kong corporation financing the project and the GRA. CIF was contracted to rebuild this rail link in exchange for oil, but CIF,s use of a high price per barrel for barter and its miscalculations of operating costs have left it financially strapped. CIF,s management-ordered work stoppage may be a plea to both the GRA and the GOC for a bail out, but the company's plight highlights the difficulties that some Chinese companies are having doing business in Angola. End Summary.

Linking Angola by Rail

¶2. (U) Background: During Angola,s colonial period three major rail lines traversed Angola, all in East-West directions. The northernmost line linked the port of Luanda with Malanje; the central line linked the port of Lobito with Zambia and Congo and was used to transport copper and other minerals; the southernmost line linked the port of Namibe with Lubango and eastern Huila province, a rich cattle and agricultural area. All the lines suffered extensive damage during the civil war and were heavily land mined. The GRA is currently demining the rail beds and repairing the lines, principally by using Chinese companies financed through the Chinese line of credit for the rail reconstruction. Embassy Luanda,s Chinese-speaking Econoff and P/E Intern traveled to Ndalatando in Kwanza Norte Province to observe the work on the Malanje railway from June 19-20, 2007.

Work Stoppage on the Malanje Rail Line

¶3. (SBU) The Luanda-Malanje line now reaches from 60 kilometers east of Luanda to within 40 kilometers of N,Dalatando, capital of Kwanza Norte Province. Construction teams are pushing toward each other from Malanje and N,Dalatando. Econoff was not able to access most stretches of rail line because of no direct access from the road to the rail line. However, he examined the line where it parallels the Luanda-N,Dalatando road and found a visible waviness to the rails at several points, as though the track bed had settled and slightly bent the rails after the line was laid.

¶4. (C) In N,Dalatando, Econoff found the supervisor of crews laying track between Dondo and N,Dalatando, Mr. Li, at the

N,Dalatando train station, which serves as a temporary dormitory and workshop for the Brigade. Li explained to Econoff that his team recently stopped its work because the Angolan government was experiencing &financial problems.8 His Chinese workers, he explained, had not been paid in eight months. At 1:30 p.m. on a Tuesday Li and four colleagues welcomed their unexpected visitor. The only person visibly doing any work was the cook, who was washing pots. Li said that he hoped work would resume as soon as Monday, June 25. He added that he normally employs 2,000 Angolan day laborers but has let them go until work can resume. By contrast, Governor Henrique Andre Junior of Kwanza Norte Province, meeting with Emboffs on June 19, said that as far as he knew, the work was underway.

Poor Calculations, Underestimated Costs

¶5. (C) Sources in Angola,s Chinese community had told Post that financial difficulties have slowed progress on rebuilding the rail line from Luanda to Malanje and that work recently had stopped altogether. The 20th Railroad Construction Brigade has a contract with Hong Kong-based China International Fund (CIF) to rebuild the line, but both CIF and the Brigade underestimated the cost of doing business in Angola. The Brigade took on the Angola project because of its experience with operating in some of China,s worst environments. Angola, however, surpassed anything in the Brigade,s experience. Among the problems: lengthy port clearance times for building materials and slow land mine clearance along the right-of-way. Higher operating costs forced it first to reduce the scale of its operations and now to stop work.

¶6. (C) A lot of finger-pointing is underway to cast blame for what may have become a bad business decision. Liu Daiwen, the former Angolan resident Deputy Manager of the Brigade, complained that CIF,s founder, Mr. Xu Jinghua,

misrepresented how much the Brigade could earn in Angola. Higher-than-expected costs then forced the Brigade to reduce its expatriate Chinese workers from 1,000 in 2006 to fewer than 300 as of June 2007. Meanwhile, Liu,s responsibility for the decision to come to Angola damaged his career and forced him to return to China in late 2006. However, Luanda sources suggest that Liu,s judgment of Xu may be too harsh. Liu,s own actions did him and CIF damage, as well.

¶7. (C) China International Fund (CIF) financial plight is also due to major miscalculation regarding the price of oil. CIF is the only Chinese company, according to our Chinese interlocutors, to directly barter its services for oil. In making its oil-for-work deal CIF apparently calculated too high, using an oil price of USD 70 per barrel. (By comparison, the GRA used USD 50 per barrel in drawing up its 2007 budget.) CIF's other project, a 24-story office complex in Luanda, is not stopped, however and may have used a different financing scheme. CIF, according to interlocutors, is hoping for a new infusion of cash from both the Government of China, betting that the GOC does not want one of its major overseas investors and large-scale employers to fail, and from the GRA, which wants its railway built.

The Mechanics of the Chinese Line of Credit

¶8. (SBU) Most Chinese firms working in Angola get paid through the Chinese line of credit to Angola: they submit invoices for work completed under their contract with the Office of National Reconstruction (GRN). The GRA approves the invoices and notifies the Bank of China (BOC), which pays the firms, accounts at the BOC and adds the sums to Angola,s debt to China. Angola, which sold China USD 10 billion worth of oil in 2006, has enough money to pay for all its ongoing rehabilitation projects. Angola,s Ministry of Finance (MOF) keeps an account at the Bank of China (BOC), where China pays for the oil it buys from Angola, according

to an expatriate financial expert in Luanda. The MOF,s account serves as collateral for BOC loans to Angola.

Comment

¶9. (C) Several sources in the Chinese community here link the Brigade,s and CIF,s financial problems to CIF,s miscalculating both the cost of doing business and the price of oil. The private CIF deal with the GRA and Sonangol further complicates the picture with barter arrangements being used to swap Angolan oil for Chinese services. However, this arrangement looks far more like poor planning and verification by CIF than anything underhanded. CIF's survival and its future as a conduit for Chinese investment in Angola (as well as the future of the oil for services model) may depend on its ability to re-calculate its barter arrangement with the GRA to more accurately reflect costs and the price of oil. If CIF's deal collapses, however, it would send a clear message to potential Chinese investors that they may not be able to count on being bailed-out for bad business decisions.
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